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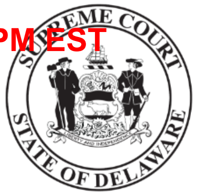

IN THE SUPREME COURT OF THE STATE OF DELAWARE

SANDRA LIFSCHITZ, HENRY FELT AND DIANE FELT, Plaintiffs Below, Appellant, v. STEVEN A. KANDARIAN, CHERYL W. GRISÉ, CARLOS M. GUTIERREZ, GERALD L. HASSELL, DAVID L. HERZOG, R. GLENN HUBBARD, EDWARD J. KELLY, III, WILLIAM E. KENNARD, JAMES M. KILTS, CATHERINE R. KINNEY, DENISE M. MORRISON, WAYNE DANIEL, STEVEN J. GOULART, JOHN C.R. HELE, JOHN M. KEANE, ALFRED F. KELLY, JR., ROBIN LENNA, MARIA R. MORRIS, HUGH B. PRICE, KENTON J. SICCHITANO, LULU WANG, and WILLIAM A. WHEELER, Defendants Below, Appellees. and METLIFE, INC., Nominal Defendant Below, Appellee.	)	C. A. No. 301,2020 Appeal from the Court of Chancery of the State of Delaware C.A. No. 2019-0452-SG

ANSWERING BRIEF OF DEFENDANTS BELOW - APPELLEES

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Dated: November 27, 2020

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NATURE OF PROCEEDINGS

This appeal challenges the Court of Chancery's order granting the motion to dismiss the Consolidated Complaint filed by Plaintiffs Below-Appellants ("Plaintiffs") asserting claims of breach of fiduciary duty, unjust enrichment and waste of corporate assets on the basis that Plaintiffs failed to make a pre-suit demand on the Board of Directors (the "Board") of MetLife, Inc. ("MetLife" or the "Company") as required by Delaware Court of Chancery Rule 23.1.[1]

Plaintiffs' claims relate to an issue disclosed by MetLife in late 2017 regarding the payment of retirement benefits under an annuity product known as a group annuity contract, or GAC. Specifically, the Company determined that its efforts to contact certain individuals who might be eligible for retirement benefits under GACs issued pursuant to pension risk transfer transactions had been inadequate. When these individuals had not responded to two letters from the Company, one sent at age 65 and one sent at age 70.5, it was presumed that they would not respond and had not become entitled to benefits, and the reserves associated with their potential claims were released (the "Group Annuities Issue").

MetLife self-reported the Group Annuities Issue in December 2017 and announced that it was reviewing and improving the processes used to locate and

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1 For purposes of this brief, the term "MetLife" includes MetLife, Inc., its subsidiaries and/or affiliates, or any of them. MetLife, Inc. is a holding company and, as such, does not enter into group annuity contracts, provide insurance or maintain insurance reserves.

contact group annuitants. MetLife's then-CEO Steven Kandarian expressed his deep regret, stating that the Company "had an operational failure that never should have happened," and the Company committed itself to finding and paying any group annuitants who were due benefits, including interest on any retroactive payments. (A96.) MetLife stated that the Group Annuities Issue would require an increase in reserves, which resulted in a $510 million charge.

The Company acknowledged its missteps and worked aggressively to remedy them. Plaintiffs' effort to convert these events into a *Caremark* claim against the Board is fundamentally flawed, however, and the Court of Chancery's order of dismissal should be affirmed. Plaintiffs filed suit without first making a demand on the Board, and the Court of Chancery correctly concluded that Plaintiffs failed to allege particularized facts demonstrating that pre-suit demand would have been futile. (Opinion 50.) Plaintiffs allege that demand is excused because a majority of the Board at the time this lawsuit was filed (the "Demand Board") face a substantial likelihood of liability on their *Caremark* claim for failure to reasonably oversee the Company's affairs – a claim often described as "possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment." *In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959, 967 (Del. Ch. 1996).

Plaintiffs' argument centers on the second prong of *Caremark* for failure to monitor, which requires Plaintiffs to allege particularized facts indicating that "the board *consciously failed to act* after learning about *evidence of illegality* – the proverbial 'red flag.'" *South v. Baker*, 62 A.3d 1, 15 (Del. Ch. 2012) (emphasis added). However, the Complaint contains no allegations indicating that any member of the Demand Board, much less a majority, had contemporaneous knowledge of MetLife's use of a two-letter process for contacting group annuitants or the practice of releasing reserves for annuitants who failed to respond to those letters. As a result, Plaintiffs cannot possibly establish as required that a "red flag" with regard to the Group Annuities Issue was "waved in [the] face" of the Board. *Wood v. Baum*, 953 A.2d 136, 143 (Del. 2008) (citation omitted). Instead, Plaintiffs base their "red flag" allegations on (*i*) state regulatory inquiries in 2011 (the "Regulatory Activity") and a Regulatory Settlement Agreement in 2012 (the "RSA") that concerned an entirely different issue, and (*ii*) a September 2016 report by MetLife's internal auditor to the Audit Committee (the "Internal Auditor's Report") that does not discuss the adequacy of the two-letter process or mention the corresponding release of reserves. To conclude that these events constituted "red flags" with regard to the Group Annuities Issue would require a set of inferential leaps far beyond the bounds of any *Caremark* precedent.

First, Plaintiffs' argument that the 2011 Regulatory Activity and 2012 RSA constitute a red flag with regard to the Group Annuities Issue fails because the 2011/2012 issues involved a different line of business, different product, different operational issue, and different type of reserve from the Group Annuities Issue. The former concerned death benefits; the latter, annuity benefits that are contingent on being alive. The former concerned use of the Social Security Administration's Death Master File (the "DMF") to identify potentially deceased policyholders; the latter concerned the release of reserves based on an annuitant's failure to respond to two letters, allegedly without additional address research or outreach efforts. The issues simply are not the same.

Furthermore, in asking the Court to infer that the 2011-2012 regulatory issues put the Demand Board on notice of the Group Annuities Issue, Plaintiffs ask the Court to overlook numerous factors suggesting the opposite, including that (*i*) the RSA is not alleged to have applied to the group annuities at issue; (*ii*) the Demand Board is not alleged to have known of the two-letter outreach process underlying the Group Annuities Issue; (*iii*) the Demand Board is not alleged to have known that the Company was relying on non-response to those two letters to release reserves for certain group annuitants; and (*iv*) the Demand Board is not even alleged to have been aware of the 2011-2012 regulatory issues. Plaintiffs' suggestion that the group annuities at issue were carved out of the RSA in order to

permit the Company to perpetuate the Group Annuities Issue is pure fiction unsupported by any well-pled facts. The "common sense" inference that Plaintiffs ask the Court to make boils down to substituting Plaintiffs' hindsight-based judgment for that of the Board and would strain *Caremark* past its breaking point.

Second, Plaintiffs' argument that the 2016 Internal Auditor's Report constituted a red flag regarding the Group Annuities Issue fails for the simple reason that the report makes no mention of that issue. The report includes brief reference to unspecified control weaknesses and expresses confidence that management is addressing those issues. It raises no concern regarding the adequacy of the two-letter process as a means of notifying group annuitants that they might be eligible for benefits and makes no mention of reserves, much less whether the lack of a response to two letters is a sufficient basis to release reserves. A report that does not even mention the issue that later came to light cannot constitute a "red flag" within the meaning of *Caremark*. Furthermore, only three members of the Demand Board were members of the Audit Committee when the Internal Auditor's Report was discussed, and Plaintiffs do not allege facts indicating that this item was discussed with the full Board.

Unable to allege any such facts, Plaintiffs offer a half-hearted argument, under the first prong of *Caremark*, that the Audit Committee's decision not to discuss this particular item from the Internal Auditor's Report somehow means that

the Board "utterly failed to implement any reporting or information system or controls." *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006). That alternative theory is unsupported by Delaware law and, as the Court of Chancery noted, undermined by Plaintiffs' own allegations regarding MetLife's "extensive network of internal controls." (Opinion 37.)

For these reasons, this Court should affirm the Court of Chancery's order of dismissal.

SUMMARY OF ARGUMENT

1. *Denied*. The Court of Chancery correctly concluded that Plaintiffs failed to alleged particularized facts demonstrating that a majority of the Demand Board were not disinterested because they face a substantial likelihood of liability for lack of corporate oversight under *Caremark* and its progeny. Plaintiffs failed to meet their burden of pleading that any of the Defendants, much less a majority of the Demand Board, was presented with "red flags" indicating illegal conduct and consciously failed to act. (Opinion 50.)

2. *Denied*. The Court of Chancery correctly concluded that Plaintiffs failed to allege any facts indicating that the Board was aware of the Group Annuities Issue – *i.e.*, MetLife's use of a two-letter process for contacting group annuitants or the practice of releasing reserves for annuitants who failed to respond to the Company's outreach efforts. (*Id*.)

3. *Denied*. The Court of Chancery correctly concluded that Plaintiffs failed to allege that a majority of the Demand Board had actual knowledge of the 2011 regulatory activity and the 2012 RSA and – more importantly – that those events were not "red flags" with respect to the Group Annuities Issue on which Plaintiffs' claims are based. (*Id*. 41, 43.)

4. *Denied*. The Court of Chancery correctly concluded that Plaintiffs failed to allege particularized facts demonstrating that a majority of the Demand

Board was aware of the Internal Auditor's Report, and that there is no basis to infer Board knowledge in the absence of such factual allegations. (*Id*. 47, 49-50.) Nor, in any event, would anything in the Internal Auditor's Report put a director on notice of the Group Annuities Issue. The Court of Chancery also correctly concluded that Plaintiffs failed to plead a claim under the first prong of *Caremark*, which would require that MetLife's Board "utterly failed to implement any reporting or information system or controls." (Opinion 37, n. 187 (quoting *Stone*, 911 A.2d at 370), n. 188.)

STATEMENT OF FACTS[2]

A. METLIFE, INC. AND ITS BOARD OF DIRECTORS

Nominal Defendant MetLife, Inc., a Delaware corporation headquartered in New York, is a holding company. (A37.) Its operating subsidiaries provide insurance and other financial services for individuals and institutions. (A50.) At the time this action was commenced, the Board was composed of one executive director – Michel A. Khalaf, President and CEO of MetLife, Inc. – and eleven independent, non-executive directors: Cheryl W. Grisé, Carlos M. Gutierrez, Gerald L. Hassel, David L. Herzog, R. Glenn Hubbard, Edward J. Kelly III, William E. Kennard, James M. Kilts, Catherine R. Kinney, Denise M. Morrison and Diana McKenzie. (A32-34.) These individuals are referred to as the "Demand Board."

Steven A. Kandarian, former MetLife President and Chief Executive Officer, left MetLife's Board on April 30, 2019. (A35.) Thus, contrary to Plaintiffs' allegations, Kandarian was not a "current" member of MetLife's Board at the time this suit was filed and is not a relevant player for the demand futility analysis. (A112; A114; A118.) Defendants Hugh B. Price, Kenton J. Sicchitano, Alfred F. Kelly, Jr., Lulu Wang, and John M. Keane are also former members of

[2] The factual allegations in the Complaint are taken as true solely for purposes of Defendants' motion to dismiss.

the Board (A34.) Collectively, Kandarian, Price, Sicchitano, Alfred Kelly, Wang, and Keane are referred to as "Former Directors."

The Current Directors, with the exception of Khalaf, Hassell[3] and McKenzie, who are not named as defendants, and the Former Directors are referred to collectively as the "Director Defendants."

Defendants John C.R. Hele, Maria R. Morris, Steven J. Goulart, and William J. Wheeler are current or former officers of MetLife and referred to as the "Officer Defendants." (A35-37.) Although Plaintiffs refer to Robin Lenna and Wayne Daniel as "officers," those individuals have never served as officers of MetLife, Inc. (A36-37.) Lenna and Daniel are referred to as the "Non-Officer Defendants."

B. PLAINTIFFS' CLAIMS

Plaintiffs' claims relate to an issue reported by MetLife in December 2017 regarding the payment of group annuity benefits flowing from MetLife's pension risk transfer business. (A50-58.) "Pension risk transfer" refers to the process by which MetLife acquires an employer's pension plans, converts those plans into group annuity contracts, and assumes both the assets and obligations associated with managing the payment of pension benefits to eligible employees. (A50-52.)

In order to initiate the payment process for annuitants who became eligible for pension benefits under the group annuity contracts, MetLife historically – until

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[3] Although listed in the caption of Plaintiffs' Brief, Gerald L. Hassell is not a defendant in this litigation. (A34.)

December of 2017 – relied, in part, on a series of mailings. (A55.) MetLife would ordinarily send the first letter when the annuitant turned 65 years old, representing the average retirement age. (A55.) If MetLife did not receive a response, MetLife assumed the annuitant was deferring his or her pension benefits beyond the normal retirement date. (A56.) MetLife would then send a second letter to the annuitant when he or she turned 70.5 years of age. (A55.) If MetLife did not receive a response to that second letter, it presumed that the annuitant would not respond and was not entitled to benefits, and it released the group annuity reserve associated with that annuitant. (A56-57.)

When MetLife reported the Group Annuities Issue in December 2017, it announced that it was reviewing and enhancing its processes used to locate and contact group annuitants. (A89.) In subsequent disclosures, MetLife stated that resolving the issue would require an increase in reserves, which resulted in a $510 million charge. (A100-02.)

C. PLAINTIFFS' DEMAND FUTILITY ALLEGATIONS

Plaintiffs did not make a pre-litigation demand on MetLife's Board prior to initiating suit as required under Delaware law and instead assert that demand would have been futile. (A112.) Specifically, Plaintiffs contend that a majority of the Demand Board faces a substantial likelihood of personal liability for failing to act in the face of purported "red flags" indicating illegality in connection with the

Group Annuities Issue. Although Plaintiffs originally alleged seven red flags to the Board, they have abandoned all but two of them for purposes of their appeal: (*i*) the 2011 Regulatory Activity and the 2012 Regulatory Settlement Agreement, and (*ii*) the 2016 Internal Auditor's Report.[4]

1. The 2011 Regulatory Activity and 2012 RSA.

Beginning in 2008, various states began to conduct inquiries into the life insurance industry's compliance with unclaimed property laws, and in particular its use of the DMF, which contains a list of deaths that have been reported to that government agency. (A62-66.) Much like the Social Security Administration itself, MetLife had used the DMF in its annuity business to ensure that the Company did not send annuity payments to deceased annuitants. (A64-66.) In its life insurance business, by contrast, MetLife and other insurers relied on beneficiaries to report the deaths of insured individuals and file claim for death benefits, in accordance with standard life insurance policies.

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[4] Plaintiffs refer twice in passing to MetLife's Pilot Program in the "Summary of Argument" and "Statement of Facts" sections of their Opening Brief. (App. Br. 6, 8.) However, Plaintiffs fail to include any actual arguments as to the Pilot Program – and whether or not it constitutes a red flag – in the remainder of their Opening Brief. Accordingly, the Pilot Program and Plaintiffs' related arguments raised in their earlier briefings are not properly before this Court on appeal. *See* Supr. Ct. R. 14(b)(vi)(A)(3) ("The merits of any argument that is not raised in the body of the opening brief shall be deemed waived and will not be considered by the Court on appeal."). Nevertheless, the Pilot Program was not a red flag because the Board learned of the "Pilot Program's findings in January, 2018, just after the Company filed the form 8-K identifying" the issue. (Opinion at 49.)

In connection with the state inquiries, MetLife officers testified at hearings in May 2011 before the Florida Insurance Commissioner and the California Insurance Commissioner regarding the Company's use of the DMF (A62-66, A182-319, A321-448), including its decision in 2010 to begin using the DMF across all business lines at least annually as a "safety net" to identify instances where an insured has died and no claim for benefits is filed (A254). There was no testimony regarding the process of locating group annuitants to begin annuity payments or the practice of releasing reserves for annuitants who did not respond to outreach efforts. (A182-319, A321-448.)

In July 2011, the New York State Department of Financial Services ("NYDFS") issued a letter pursuant to Section 308 of the New York Insurance Law to the hundreds of insurers doing business in New York directing insurers to cross-check policy records against the DMF. (A27, A59-61.) In December 2011, the NYDFS issued an interim report reiterating that insurance companies should use the DMF to "determine if any death benefit payments are due under life insurance policies, annuity contracts, or retained asset accounts." (A60.) The NYDFS did not address the process of locating group annuitants to begin annuity payments or the practice of releasing reserves for annuitants who did not respond to outreach efforts. Plaintiffs do not, and cannot, allege that the December 2011 report found that any company was in violation of any laws or regulations.

In April 2012, MetLife entered into the RSA with multiple states. (A68, A160-180.) In the RSA, MetLife agreed to implement changes for its procedures relating to the payment of death benefits, including periodic cross-checks of life insurance and annuity policies against the DMF and a "thorough search" process to locate beneficiaries. (A160-180.) MetLife agreed to accelerate the escheatment of $438 million in unclaimed benefits and to pay $40 million to the states to cover the cost of the investigation. (A71.) In connection with the RSA, MetLife expressly denied any wrongdoing or any violation of law, and the parties agreed that the RSA may not be deemed to be "an admission of or evidence of liability or any wrongdoing by the Company." (A162, 171.) The RSA did not apply to the group annuity contracts at issue in this case. (A73.) As the Court of Chancery aptly summarized, "[n]othing in the investigations or the RSA put those who became aware of them on direct notice of deficiencies in the Pension Risk Transfer Business and its tracking of annuitants." (Opinion 41.)

2. The September 2016 Internal Auditor's Report to the Audit Committee.

The September 2016 Internal Auditor's Report was presented to the Audit Committee and summarizes Internal Audit's activities in the second quarter of

2016. (A522.)[5] The Internal Auditor's Report included only a general reference to "control weaknesses over several areas, including contract accuracy, manual certificate mailings, and retirement letter mailings (e.g. age 65 and 70.5)." It did not mention any concerns regarding the use of the mailings as a means of contacting annuitants or the release of group annuity reserves. (A521-32.) Contrary to Plaintiffs' suggestion, the identified "control weaknesses" were not deemed to be "material." (App. Br. 20, 36, 45.) The Internal Auditor's Report also made clear that any control weaknesses were not being ignored: "Management is in the process of making enhancements, including improving contract accuracy and improving the manual participant certificate mailing and retirement notification mailing." (A526.) It also stated that Internal Audit was "satisfied that management's action plans will mitigate the issues raised in these audits." (A522.)

The portion of the Internal Auditor's Report on which Plaintiffs rely purports to summarize a June 29, 2016 Audit Report, which provides detail regarding the identified "control weaknesses." (B62.)[6] The June 2016 Audit Report, which is publicly available but entirely ignored by Plaintiffs, confirms that

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[5] Plaintiffs submitted the relevant excerpts of the Internal Auditor's Report to the Court of Chancery on May 4, 2020, after briefing on the motion to dismiss was complete and in advance of oral argument. (A516-32.)

[6] Following oral argument and at the Court of Chancery's invitation, Defendants' submitted the June 2016 Audit Report to the Court of Chancery. (A629-30; A635-36; B58-64.)

the control weaknesses referred to on the page of the Internal Auditor's Report cited by Plaintiffs are not what gave rise to the Group Annuities Issue. Instead, the control weaknesses at issues were based on findings that "retirement notification letters" were "not always sent," due in part to MetLife's then-recent transition to a new administrative platform. (B59; B62.) The June 2016 Audit Report goes on to detail the "Management Action Plan," which included manual mailings during the transition and confirmation that letters were mailed. (B62.) Like the Internal Auditor's Report, the June 2016 Audit Report does not raise any concerns regarding the use of the two-letter process to contact annuitants or the release of group annuity reserves.

Only three of the twelve members of the Demand Board attended the September 2016 Audit Committee meeting at which the Internal Audit Report was presented. (A82.) There are no factual allegations indicating that the remaining directors of the Demand Board were made aware of it. (A490.)

D. THE COURT OF CHANCERY DISMISSED PLAINTIFFS' COMPLAINT FOR FAILURE TO ADEQUATELY PLEAD DEMAND FUTILITY

On August 17, 2020, the Court of Chancery granted Defendants' motion to dismiss on the ground that Plaintiffs failed to plead sufficient facts to excuse demand under Rule 23.1. The Court of Chancery found that Plaintiffs failed to

offer "specific factual allegations from which [the court] can reasonably infer that the Board was aware of red flags and ignored them in bad faith." (Opinion 50.)

Specifically, the Court of Chancery found that Plaintiffs could not rely on the 2011 Regulatory Activity and 2012 RSA because those events were not "red flags" with respect to the Group Annuities Issue on which Plaintiffs' claims are based, and Plaintiffs also failed to adequately allege that a majority of the Demand Board had actual knowledge of them. (*Id.* 41, 43.) The Court of Chancery similarly found that "the implication of bad faith is absent" from Plaintiffs' allegations regarding the 2016 Internal Auditor's Report and, in any event, it was presented to "only a minority of the Demand Board." (*Id*. 50 n.228.) Plaintiffs therefore failed to adequately plead a substantial likelihood of liability under *Caremark*.

Because Plaintiffs' claims for unjust enrichment and corporate waste are premised entirely on the *Caremark* claim, the Court of Chancery found that "the same result" was warranted and determined the "Demand Board is capable of reviewing" all of Plaintiffs' claims. (*Id.* 51-52.)

On July 27, 2020, Magistrate Judge Jennifer L. Hall issued a Report and Recommendation in a parallel case, *Kates v. Kandarian*, pending in the United States District Court for the District of Delaware, which was subsequently adopted by the District Court. (B65-91; B92-93.) Judge Hall recommended that the federal

securities claims be dismissed for failure to state a claim and that the court decline to exercise jurisdiction over the *Caremark* claims. (B87, B89.)

Judge Hall's analysis of scienter is highly relevant to the *Caremark* analysis, as it also relies on a theory of "red flags." In particular, Judge Hall rejected the 2011 Regulatory Activity and 2012 RSA as evidence of knowledge of the Group Annuities Issue, finding that they "*dealt with a different issue*, namely, MetLife's procedure for identifying . . . beneficiaries entitled to death benefits." (B82 (emphasis added).) Furthermore, she correctly observed that the 2016 internal audit report "*makes no mention* of any issues relating to MetLife's use of the two-letter procedure to identify and locate living pension annuitants" and if anything, "weighs *against* an inference of scienter" because it contained a management plan to address any weaknesses identified. (B83-84 (emphasis added).)

ARGUMENT

Plaintiffs failed to allege particularized facts showing that a majority of the Board consciously failed to act in the face of red flags of illegality.

I. QUESTION PRESENTED

Did the Court of Chancery correctly conclude that pre-suit demand was not excused because Plaintiffs failed to allege with particularity that the Board consciously disregarded red flags of illegal conduct with regard to the Group Annuities Issue? (B16-30; B42-50.)

II. SCOPE OF REVIEW

This Court reviews "*de novo* the decision of the Court of Chancery to dismiss a derivative suit under Rule 23.1." *White v. Panic*, 783 A.2d 543, 549 (Del. 2001). It is established that a stockholder may not commence derivative litigation on behalf of a corporation unless the stockholder (*i*) first makes a pre-suit demand upon the board to commence an action on behalf of the company (and the board wrongfully refuses to do so) or (*ii*) pleads *particularized factual allegations* demonstrating that a demand would be "futile" because a majority of the board is incapable of making a disinterested and independent judgment as to whether the corporation should pursue the claims. *Rales v. Blasband*, 634 A.2d 927, 932-934 (Del. 1993), *abrogated on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000) (emphasis added); Del. Ct. Ch. R. 23.1.

Delaware law imposes an "onerous" burden on a plaintiff who alleges that pre-suit demand would be futile. *Levine v. Smith*, 591 A.2d 194, 207 (Del. 1991), *abrogated on other grounds by Brehm*, 746 A.2d 244. Where, as here, the subject of a lawsuit is board inaction, demand is excused as futile "only if *a majority of the directors* have such a personal stake in the matter at issue or the proposed litigation that they would not be able to make a proper business judgment in response to a demand." *In re Dow Chem. Co. Deriv. Litig.*, 2010 WL 66769, at *6 (Del. Ch. Jan. 11, 2010) (emphasis added).

Plaintiffs bear the burden of pleading with particularity facts showing that any effort to make a demand would be futile. Del. Ct. Ch. R. 23.1. While the Court may draw reasonable inferences in Plaintiffs' favor, "[c]onclusory allegations are not considered as expressly pleaded facts or factual inferences [and] inferences that are not objectively reasonable cannot be drawn in plaintiff[s'] favor." *Wood*, 953 A.2d at 140 (quotation marks and citations omitted).

III. MERITS OF ARGUMENT

Although Plaintiffs base their demand-futility allegations on a theory that the Board ignored "red flags" indicating illegal conduct, thereby "consciously permitting the corporation to violate positive law," *South*, 62 A.3d at 6, 16, the Complaint contains no allegations indicating that any of the Director Defendants had contemporaneous knowledge of the Group Annuities Issue. There are no

allegations indicating that the Board was aware that MetLife's outreach to individuals entitled to pension annuity benefits consisted of two letters, much less that the Company relied on a lack of response to those letters to release reserves.

Instead, Plaintiffs base their red-flag allegations on a theory that the Board "should have known" of the Group Annuities Issue. This argument is based on (*i*) the 2011 Regulatory Activity and 2012 RSA, and (*ii*) a 2016 Internal Audit Report. The former concerned an entirely different issue from the Group Annuities Issue – namely, use of the DMF to identify potentially deceased policyholders to facilitate the payment or escheatment of unclaimed life insurance benefits – and reflected a change in applicable law rather than a violation. The latter did not address the adequacy of the two-letter process or the corresponding release of reserves. *Caremark* is not a vehicle for substituting Plaintiffs' hindsight-based views of what the Board "should have" done for the Board's real-time judgment. To conclude that these events constituted red flags with regard to the Group Annuities Issue would require a set of inferential leaps far beyond the bounds of the law.

A. Plaintiffs Fail to Plead Demand Futility Based on the 2011 Regulatory Activity and 2012 RSA.

1. The 2011 Regulatory Activity and 2012 RSA Did Not Put the Board on Notice of the Group Annuities Issue.

Plaintiffs fail to allege particularized facts indicating that the 2011 Regulatory Activity and the 2012 RSA put the Board on notice of inadequacies with the Company's procedures for releasing reserves with regard to pension annuitants. As discussed above, the 2011/2012 events concerned the use of the DMF to help determine whether any policyholders had died in order to identify potentially unclaimed *death benefits*. The Group Annuities Issue, by contrast, involved the practice of releasing group annuity reserves based on allegedly inadequate processes for contacting pension annuitants for the purpose of making *life-contingent* payments – *i.e.*, payments that are only owed if the annuitant or beneficiary is alive. The former involved the use of the DMF rather than awaiting the submission of death claims as had historically been done; the latter involved additional mailings, certified mailings, phone calls and the use of additional third-party firms specializing in locating unresponsive participants. The Group Annuities Issue involved a different line of business, different procedures, and different types of reserves from the 2011/2012 events.

For these reasons, the Court of Chancery correctly recognized that the 2011 Regulatory Activity and 2012 RSA addressed different lines of business within

MetLife and therefore could constitute red flags with respect to the Group Annuities Issue. (Opinion 41 (emphasis added).)[7] The *Kates* court likewise rejected the argument that the 2011 Regulatory Activity and 2012 RSA were evidence of scienter, finding that "they dealt with a different issue, namely, MetLife's procedure for identifying . . . beneficiaries entitled to death benefits." (B82.)

In addition, Plaintiffs' allegation that the RSA did not apply to the group annuities at issue precludes any inference that the RSA put the Board directly on notice of the Group Annuities Issue. (App. Br. 18-19; A73-74.) Perhaps recognizing this issue, Plaintiffs attempt to salvage their claims by converting that carve-out into a scienter allegation. But the suggestion that MetLife "purposefully" negotiated with regulators to exclude pension annuities from the scope of the RSA while knowing that the two-letter process was inadequate, presumably with a goal of facilitating improper releases of reserves, with the

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[7] The Court of Chancery further found that, while it viewed the life insurance and pension risk transfer lines of business as "analogous," a failure to "recognize that use of the DMF in one way in one line of business made it wise to use it differently in another . . . does not thereby also imply bad faith." (*Id.* 41-42.) While MetLife agrees with the Court of Chancery's conclusion that Plaintiffs have not successfully alleged bad faith, MetLife respectfully disagrees that the lines of business are analogous for purposes of a *Caremark* analysis and notes that, despite Plaintiffs' scouring of MetLife's public statements and Section 220 materials regarding the Group Annuities Issue, there are no well-pled facts to suggest that the Company's use or non-use of the DMF was a driver of the Group Annuities Issue.

"highly likely" approval by the Company's then-board, is a made-up conspiracy theory unsupported by a single well-pled fact. (App. Br. 19.) Given the scope of the regulatory investigation that Plaintiffs describe, the inference Plaintiffs seek that the Company defrauded its regulators is not reasonable. Plaintiffs cannot plead a *Caremark* claim based on insinuation.

While Plaintiffs attempt to draw parallels between the 2011/2012 events and the Group Annuities Issue, Plaintiffs allege no facts indicating that the Board was aware of the specific two-letter practice in use in the pension annuity business, much less that the Company was relying on a lack of response to those letters to release reserves – the issue at the heart of the Group Annuities Issue. (B82 (finding allegations insufficient to suggest that MetLife's Board of Directors knew prior to 2017 that "MetLife even used the two-letter procedure to determine which pension annuitants were alive," much less that they were aware of any deficiencies in the process and chose to ignore them).) The RSA sets out procedures for the Company to apply going forward in certain lines of business, but it does not address reserves at all. Nothing about the RSA would put the Board on notice of a risk that reserves were being released without adequate controls.

2. The 2011 Regulatory Activity and 2012 RSA Did Not Indicate Ongoing Violations of Positive Law.

Plaintiffs' assertion that the Regulatory Activity and RSA meant that MetLife had violated "positive law" is both irrelevant – because those events

address a different matter from the Group Annuities Issue – and incorrect. Contrary to Plaintiffs' suggestion, the Regulatory Activity did not involve a finding that MetLife had violated any legal obligation. The NYDFS Interim Report upon which Plaintiffs rely merely described learnings from an industry-wide inquiry; it did not find that any company had violated existing law. (App. Br. 14-16; A59-60.) Plaintiffs do not, and cannot, cite any language from that report (or the earlier Section 308 letter) that identifies any violations of law.

Nor did the RSA "denote violations of positive law" as Plaintiffs assert. (App. Br. 26.) MetLife did not admit any liability or wrongdoing as part of the 2012 RSA. (Opinion 41.) The parties explicitly agreed that "[n]either [the] Agreement, nor any act performed or document executed pursuant to or in furtherance of this Agreement, is now or may be deemed in the future to be an admission of or evidence of liability or any wrongdoing by [the] Company . . . ." (A171.) Contrary to Plaintiffs' assertion, the RSA's introductory "WHEREAS" clauses stating that regulators "identified concerns" regarding aspects of the Company's practices are not a finding that the Company violated positive law. (App. Br. 26.) The WHEREAS clauses likewise state that MetLife "has policies and procedures to ensure the payment of valid claims" and to report unclaimed property, and that MetLife "denies any wrongdoing or any violation of the Unclaimed Property Laws or the Insurance Laws of any of the Signatory States or

any other applicable law." (A161-62.) An expression of concern that is disputed by the Company does not amount to a finding that the practices at issue were, in fact, unlawful. (*See id*.)

Even if the RSA had denoted violations of positive law, however, that would not make it a red flag within the meaning of *Caremark*. Plaintiffs would have to allege particularized facts putting the Demand Board on notice of an *ongoing* violation of law. *See Rojas v. Ellison*, 2019 WL 3408812, at *11 (Del. Ch. July 29, 2019) (dismissing *Caremark* claim where plaintiff failed to allege "particularized facts from which it reasonably can be inferred" that a class action settlement "put the directors on notice of any ongoing violations of law").

The RSA resolved disputed regulatory matters and laid out procedures going forward, but it did not apply to the Group Annuities Issue. (A73.) As a result, Plaintiffs have not identified any violation of the RSA. *Rojas*, 2019 WL 3408812, at *14 (finding settlement not a red flag in absence of any well-pled allegations that the Board "ever became aware that the Company failed to implement the procedures required" under the settlement); *Horman v. Abney*, 2017 WL 242 571, at *11 (Del. Ch. Jan. 19, 2017) (finding regulatory settlement not a red flag where Plaintiffs failed to allege the company thereafter continued to act in violation of the settlement).

3. Plaintiffs Do Not Allege That a Majority of the Demand Board Had Knowledge of Any Red Flag Related to the Regulatory Activity or RSA.

As the Court of Chancery correctly noted, even if aspects of the Regulatory Activity or the RSA could be deemed red flags with regard to the Group Annuities Issue (which they are not), "there are insufficient allegations from which [the court] may infer that knowledge of such was presented to the Director Defendants themselves." (Opinion 43.)

Only four members of the 2012 board were on the Demand Board six years later. (B15.) Plaintiffs have failed to include any particularized allegations that a majority of the Demand Board was even aware of the 2011 Regulatory Activity and 2012 RSA – let alone aware of any facts about those events that raised a red flag with regard to the Group Annuities Issue that the Demand Board ignored in bad faith.[8] Plaintiffs do not allege that the Demand Board had knowledge of the two-letter procedure at issue or how that process intersected with group annuity reserves. And even assuming Plaintiffs had alleged particularized facts indicating that the Board was generally aware of the 2011 Regulatory Activity and 2012 RSA

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[8] Plaintiffs argue that four Board members had actual knowledge of the 2012 RSA because they were named as defendants in a federal class action in the Southern District of New York. But Plaintiffs do not allege any facts sufficient to enable the Court to evaluate the relevance – or lack thereof – of that lawsuit to the Group Annuities Issue. Their conclusory assertion that the allegations are "essentially the same" (A114) is not a sufficient basis for the Court to find that the lawsuit, which is public and in fact has nothing to do with the Group Annuities Issue, constituted a red flag. (App. Br. 32.)

(which they have not), Plaintiffs do not allege facts indicating that either the Regulatory Activity or the RSA put the Demand Board on notice of control weaknesses with regard to the release of reserves related to pension risk transfer deals.

Instead, Plaintiffs rely on a theory of constructive knowledge that turns applicable law on its head. Plaintiffs argue that the "core principle of red flags" is "that when displayed, red flags are observed by those who are charged with overseeing a company's regulatory compliance." (App. Br. 31-32). In other words, if a red flag exists, the Board is deemed to have seen it. This Court has made clear, however, that "red flags are only useful when they are either waved in one's face or displayed so that they are visible to the careful observer." *Wood*, 953 A.2d at 143 (internal quotation omitted); *see also Forsythe v. ESC Fund Mgmt. Co. (U.S.)*, 2007 WL 2982247, at *7 (Del. Ch. Oct. 9, 2007) ("[D]irectors will be potentially liable for breach of their oversight duty only if they ignore 'red flags' that actually come to their attention."). Delaware courts "routinely reject the conclusory allegation that because illegal behavior occurred, internal controls must have been deficient and the board must have known so." *Horman*, 2017 WL 242571, at *7 (quoting *Desimone v. Barrows*, 924 A.2d 908, 940 (Del. Ch. 2007)) (cited in Opinion 42).

4. Plaintiffs' Argument Requires an Impermissible String of Inferences Unsupported by Delaware Law.

Plaintiffs' argument that the 2011-2012 events were a red flag as to the Group Annuities Issue relies on a series of inferences that are not supported by particularized factual allegations and would stretch *Caremark* beyond recognition. Plaintiffs ask the Court to infer among other things (*i*) that the Regulatory Activity and RSA reflected violations of positive law with regard to certain lines of business, notwithstanding that no such violations were found or admitted; (*ii*) that a majority of the Demand Board was aware of the 2011 Regulatory Activity and 2012 RSA six or more years after the fact, notwithstanding the absence of allegations to support such knowledge; (*iii*) that a majority of the Demand Board believed that the 2011 Regulatory Activity and 2012 RSA meant that there were ongoing violations of positive law with respect to a *different* process in a *different* area of the business; (*iv*) that a majority of the Demand Board reached this conclusion notwithstanding the lack of any factual allegations indicating that the Demand Board had knowledge of the two-letter process or reserve-release issue underlying the Group Annuities Issue; and (*v*) that the "absence of reform" to the Company's procedures for paying group annuity benefits amounted to bad faith, as is required for a *Caremark* claim. (Opinion 45-46; *see also* App. Br. 31-33.)

As the Court of Chancery correctly held, this line of inferences cannot "hold up under the demanding Rule 23.1 analysis, which requires specific factual

allegations in order to draw an inference of bad faith on the part of directors." (Opinion 46.) By relying on this chain of inferences, Plaintiffs fail to meet their "onerous" burden to demonstrate that pre-suit demand would be futile, *see Levine*, 591 A.2d at 207, because these "conclusory allegations are not considered as expressly pleaded facts or factual inferences." *Brehm*, 746 A.2d at 255. Drawing inferences unsupported by well-pled facts is "contrary to a well-recognized purpose of the demand futility requirement of Rule 23.1, which is to 'not permit a stockholder to cause the corporation to expend money and resources in discovery and trial in the stockholder's quixotic pursuit of a purported corporate claim based solely on conclusions, opinions or speculation.'" *Teamsters Union 25 Health Servs. & Ins. Plan v. Baiera*, 119 A.3d 44, 57-58 (Del. Ch. 2015) (quoting *Brehm*, 746 A.2d at 255); *In re Goldman Sachs Grp., Inc. S'holder Litig.*, 2011 WL 4826104, at *18 (Del. Ch. Oct. 12, 2011) ("A simple allegation of *potential* directorial liability is insufficient to excuse demand, else the demand requirement itself would be rendered toothless, and directorial control over corporate litigation would be lost.").

Plaintiffs cite no authority permitting them to establish demand futility by substituting multiple inferential leaps for particularized, well-pleaded facts. Plaintiffs' reliance on this Court's decision in *Marchand v. Barnhill*, 212 A.3d 805 (Del. 2019), is misplaced as that was not a "red flags" case at all; it was decided

under "prong one" of *Caremark*, which permits a plaintiff to state a claim under *Caremark* by alleging particularized facts indicating that a board of directors "utterly failed to implement any reporting or information system or controls." *Id*. at 808.

To the extent Plaintiffs cite "red flags" cases, those cases involved particularized factual allegations that the board was on notice of the *exact issue* that ultimately came to light, not allegations, such as those present here, that the board should have extrapolated from a different set of facts that the plaintiffs view, in hindsight, as analogous. The case of *In re Clovis Oncology Inc. Deriv. Litigation*, 2019 WL 4850188, at *15 (Del. Ch. Oct. 1. 2019), for example, involved a biopharmaceutical company with three drugs in development and none yet on the market. The Court of Chancery found that plaintiffs made particularized factual allegations demonstrating that "the Board consciously ignored red flags that revealed a mission critical failure to comply with the [clinical trial] protocol and associated FDA regulations" for the company's most promising drug in development. *Id*. In particular, plaintiffs alleged that the board was "hyper-focused" on the drug's development, spent hours discussing the progress of the clinical trials, and knew that FDA approval of the drug hinged on the drug's "objective response rate," or "ORR," which is the measure of efficacy. *Id*. at *4-5. The Court of Chancery held that plaintiffs successfully alleged that the board

ignored red flags in the form of multiple reports to the board indicating that the company was improperly calculating and reporting the ORR – the exact issue that ultimately came to light and caused the drug to be rejected by the FDA. *Id*. at *14-15.

The case of *Teamsters Local 443 Health Servs. & Ins. Plan v. Chou*, 2020 WL 5028065 at *21 (Del. Ch. Aug. 24, 2020) (referred to by Plaintiffs as "*AmerisourceBergen*") likewise involved red flags regarding the actual issue that later came to light. The case involved the operation of a criminal enterprise known as the Pre-Filled Syringe Program, in which excess amounts of oncology drugs that are normally found in pre-filled syringes were illegally extracted, pooled, and used to fill additional syringes in an unsterile environment. *Id*. at *4-8. The Court found that the plaintiffs adequately pleaded that a majority of the board was aware of the illegal conduct because they served on the board in 2010 when it disclosed the existence of a *qui tam* action – "the principal red flag alleged" – and failed to address that conduct, seven years before the Department of Justice filed a Criminal Information against the company. *Id*. at *6, *25.

For those reasons, Plaintiffs' purported "red flag" authorities provide no support for the inferential leaps that they ask this Court to make.

B. Plaintiffs Fail to Plead Demand Futility Based on the Internal Auditor's Report.

The Court of Chancery correctly concluded that Plaintiffs failed to plead demand futility based on the Internal Auditor's Report. Plaintiffs do not allege particularized facts indicating that the Internal Auditor's Report would put a director on notice of the Group Annuities Issue or that it was shown to a majority of the Demand Board. Plaintiffs' new fallback argument that they "should be allowed to proceed under prong I of *Caremark*" because the Audit Committee did not convey the full contents of the Internal Auditor's Report to the Board is unsupported by factual allegations and contrary to established Delaware law. (App. Br. 43.)

1. The Internal Auditor's Report Is Not a Red Flag.

Contrary to Plaintiffs' assertion, the Court of Chancery did not "acknowledge[] that the Auditor's Report was a timely red flag." (App. Br. 38 (citing Opinion 49).) Instead, the Court of Chancery concluded that, with respect to the Internal Auditor's Report and other purported red flags, Plaintiffs failed to "offer specific factual allegations" from which a court could "reasonably infer that the Board was aware of red flags and ignored them in bad faith." (Opinion 50.)

Plaintiffs identify nothing in the Internal Auditor's Report – a lengthy document that summarized Internal Audit's second-quarter 2016 activities – that would put a director on notice of the Group Annuities Issue. (A80-83, A520-32.)

The Internal Auditor's Report does not address the adequacy of MetLife's two-letter process for contacting group annuitants or make any mention of group annuity reserves. Instead, it included only a general reference to "control weaknesses over several areas, including contract accuracy, manual certificate mailings, and retirement letter mailings (e.g. age 65 and 70.5)." (A526.) Nothing in that statement would alert a member of the Audit Committee of the Group Annuities Issue. Plaintiffs' conclusory assertion that the Internal Auditor's Report put the Audit Committee on notice of "the control weaknesses that gave rise to this action" is unsupported by the actual document. (App. Br. 35; B83.)

Furthermore, Plaintiffs are unable to explain why the Audit Committee, upon receiving a report from MetLife's internal audit department, would have believed that any control weaknesses were being ignored. The Internal Auditor's Report explicitly stated that MetLife's management "is in the process of making enhancements" and that Internal Audit was "satisfied that management's action plans will mitigate the issues raised in these audits." (A522; A526.) Nothing about the Internal Auditor's Report suggests that control weaknesses were being ignored. (B84.)

Although the Court need go no further than the Internal Auditor's Report itself to conclude that it would not put a director on notice of the Group Annuities Issue, the underlying June 2016 Audit Report – which the Internal Auditor's

Report purports to summarize – confirms that the control weaknesses were unrelated to the Group Annuities Issue. According to the June 2016 Audit Report, which Defendants submitted at the Court of Chancery's invitation, the issue was that "retirement notification letters" were "not always sent" due in part to MetLife's then-recent transition to a new administrative platform. (B59, 62.) Nothing in the June 2016 Audit Report indicates any concern with the use of the two-letter process to contact annuitants or the practice of releasing reserves for annuitants who did not respond to its outreach efforts. (B57-64.)

Plaintiffs' attempt to tie the Internal Auditor's Report to the 2011 Regulatory Activity and 2012 RSA is misplaced because those events had nothing to do with either the Group Annuities Issue (as discussed in Section III.A.1 above) or the control weaknesses identified in the Internal Audit Report, and neither the RSA nor the Internal Auditor's Report identified any "misconduct." (App. Br. 36.) Similarly, the December 2011 statement from the NYDFS, which indicated that it was requiring all insurers to use the DMF to "identify any death benefit payments that may be due . . . as a result of the death of an insured," is unrelated to the Group Annuities Issue or the Internal Auditor's Report. (A59-60.) Plaintiffs misleadingly quote a statement from the NYDFS about the changing "protocol for finding retirees who are owed benefits," but that statement was made in December

2017 – *after* MetLife self-reported the Group Annuities Issue. (App. Br. 37; Opinion 42; A98.)

2. Plaintiffs Do Not Allege That a Majority of the Demand Board Was Aware of the Internal Auditor's Report.

Plaintiffs concede that only three of the twelve members of the Demand Board served on the Audit Committee in September 2016 when the Internal Auditor's Report was presented (App. Br. 34-35), and it therefore could not support a finding that a majority of the Demand Board face a substantial likelihood of liability. (Opinion at 50 n.228 (noting that, even if the Internal Auditor's Report were a red flag, it "would taint only a minority of the Demand Board").)

Nor is there a reasonable basis to infer that the Audit Committee communicated the specific item at issue from the Internal Auditor's Report to the full Board. As a general matter, an audit committee is not required to report to the full board every matter that is presented to it. There certainly is no reason to expect that the Audit Committee would have reported to the full Board the specific control weaknesses identified in the Internal Auditor's Report – a passing reference in a lengthy report – as Internal Audit expressed confidence that management was taking actions which would mitigate those issues. (A522, 526.) Plaintiffs themselves allege that working with Internal Audit regarding internal control over financial reporting falls squarely within the scope of the Audit Committee's authority (A39-41), and Plaintiffs concede that nothing in the books and records

produced to them indicates that the full Board was, in fact, presented with the control weaknesses identified in the Internal Auditor's Report. (App. Br. 37-38.) *See Baiera*, 119 A.3d at 57-58 (refusing to take "unsupported leap of logic" that full board was involved in review and approval process delegated to audit committee).

In asking the Court to infer, nonetheless, that the Audit Committee did communicate the control weaknesses identified in the Internal Auditor's Report to the full Board, Plaintiffs rely on two unsupported assertions. *First*, although Plaintiffs repeatedly state that the Internal Auditor's Report identified "material" weaknesses (App. Br. 20, 36, 45), the report does not characterize them as "material" and states that "the control environment is adequate." (A526.) The distinction is important because a "material weakness" indicates that "that there is a reasonable possibility that a material misstatement of the registrant's annual or interim financial statements will not be prevented or detected on a timely basis." 17 C.F.R. § 240.12b-2.

Second, Plaintiffs' assertion that the Audit Committee's charter required it to report the control weaknesses identified in the Internal Auditor's Report to the full Board is likewise unsupported by any factual allegations. (App. Br. 38 (citing A82-83).) Contrary to Plaintiffs' suggestion, the excerpts of the Audit Committee charter quoted in the Complaint do not address any obligation to report to the full

Board. (A39-41; A82-83.) In fact, the charter states only that the Audit Committee "shall make regular reports to the Board about the Committee's activities" (A640 n.3), and there is no allegation that it did not make such reports. Plaintiffs point to nothing in the charter that would obligate the Audit Committee to report to the full Board about a passing reference to control weaknesses that Internal Audit did not consider material and that were being effectively addressed by management.

Nor do the cases Plaintiffs cite support their argument. In *Wal-Mart Stores, Inc. v. Indiana Electrical Workers Pension Trust Fund IBEW*, 95 A.3d 1264 (Del. 2014), the Court affirmed the Court of Chancery's order requiring Wal-Mart to produce officer-level documents in response to a Section 220 demand but made clear that board knowledge could be inferred only where the evidence demonstrates that specific officers knew the relevant facts, were in a "reporting relationship" to directors and "did in fact report to specific directors." *Id.* at 1273. The Court expressly declined to adopt a presumption of board knowledge. *Id.* In *AmerisourceBergen*, the Court of Chancery drew an inference of board knowledge of a subpoena because it was *disclosed* in a public filing signed by the board. 2020 WL 5028065, at *24. As relevant here, the Court of Chancery held that it was "not reasonable to infer that the Board consciously ignored a red flag with regard to the search warrant, because there is no well-pled allegation that the Board had

knowledge of the search warrant or the raid, and hence the scienter required to adequately plead bad faith is absent." *Id.* The Court of Chancery's decision in *Saito v. McCall*, 2004 WL 3029876 (Del. Ch. Dec. 20, 2004), *overruled on other grounds by Lambrecht v. O'Neal*, 3 A.3d 277 (Del. 2010), is likewise inapposite as the inference of board knowledge was not based solely on alleged knowledge by members of the audit committee. *Id.* at *7.

3. Plaintiffs Do Not Allege That MetLife's Board Utterly Failed to Implement Any Reporting or Information System or Controls.

Having failed to plead that the Audit Committee apprised the full Board of the control weaknesses identified in the Internal Auditor's Report – and ignoring that those control weaknesses are completely unrelated to the Group Annuities Issue on which their claims are based – Plaintiffs fall back on the credulity-straining argument, under the first prong of *Caremark*, that MetLife's Board "utterly failed to implement any reporting or information system or controls." *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006). (App. Br. 43-45.) The Court of Chancery correctly held that, "[t]o the extent the Plaintiffs attempt to put forward a claim under *Caremark's* first prong, . . . that attempt fails." (Opinion 37.)

As the Court of Chancery correctly observed – and Plaintiffs do not dispute – it "is clear from the Complaint that MetLife had an extensive network of internal controls." (Opinion 37.) Specifically, "Plaintiffs allege[] that MetLife has an

Audit Committee, as well as a Finance and Risk Committee, and further allege that these committees meet regularly (indeed, frequently), that they have internal codes of conduct, and that the Audit Committee receives reports from MetLife's internal auditor." (Opinion 37 n.188 (citing A39-46, A80-83).) Moreover, any assertion that "the Board utterly failed to implement a reporting system" is further contradicted by Plaintiffs' allegations that other purported "red flags" – such as the results of the Pilot Program in January 2018 – "reached the Board level through internal reporting systems." (*Id.* (citing A77).) In other words, Plaintiffs specifically allege that MetLife *did* have Board-level oversight mechanisms in place. Such allegations foreclose a claim under *Caremark*'s first prong.

Plaintiffs rely almost exclusively on *Marchand v. Barnhill*, 212 A.3d 805 (Del. 2019), but that decision does not support a claim under the first prong of *Caremark* in this case. (App. Br. 44-45.) In *Marchand*, the Court held that the plaintiff met his "onerous pleading burden" because he alleged that Blue Bell Creameries USA, Inc., which manufactured ice cream, lacked *any* "compliance system and protocols" related to food safety – "the obviously most central consumer safety and legal compliance issue facing the company." 212 A.3d at 824. Blue Bell had "no board committee charged with monitoring food safety" or any process by which food safety compliance issues would be reported to the board by management. *Id.* at 813. That failure meant that the board was unaware of

critical food safety deficiencies, which ultimately led to *listeria* contamination in Blue Bell's ice cream that caused the death of three of the company's customers and injured others. *Id.* at 812-14.

The *Marchand* Court repeatedly emphasized that "*Caremark* is a tough standard for plaintiffs to meet," *id.* at 822, and it made clear that Delaware law gives great deference to boards to design appropriate reporting and information systems, which means that a prong-one *Caremark* claim must be dismissed "even when illegal or harmful company activities escaped detection," so long as the board made a "good faith effort to put a reasonable compliance and reporting system in place." *Id.* at 821. The "bottom-line requirement" of *Caremark*'s first prong is that a board must "make a good faith effort – *i.e.*, try – to put in place a reasonable board-level system of monitoring and reporting." *Id.*

Here, as the Court of Chancery noted, Plaintiffs' own allegations make clear that MetLife did have a reasonable board-level monitoring system in place. The Audit Committee's alleged decision not to escalate to the full Board certain control weaknesses – weaknesses that were not deemed material and were being addressed by management – does not come anywhere close to an utter failure by the Board to "implement any reporting or information system or controls." *Stone*, 911 A.2d at 370.

CONCLUSION

The judgment of the Court of Chancery should be affirmed.

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